1989

HOUSTON INDUSTRIES INCORPORATED

CAPITAL STRUCTURE

LONG TERM DEBT

Issue	Rating	Amount Outstanding	[2]Times Charges Earned 1988	1987	Interest Dates	Call Price	Price Range 1988	1987
1 Senior deb, 9⅝s, due 1996	Baa2	$199,329,000			F&A 15	[4]105 23	101⅓- 97	98⅛
2 Subsidiaries' debt		3,241,482,000	2 40	2 86				

SUBSIDIARY PREFERRED STOCK

Issue	Par Value	Rating	Shares Outstanding	Earned per Sh 1988	1987	Divs per Sh 1988	1987	Call Price	Price Range 1988	1987
1 Houston Lighting & Power Co, cum pfd	No Par [3]		See Text [3]	[3]	[3]	[3]		[3]	[3]	[3]

CAPITAL STOCK

Issue	Par Value	Rating	Shares Outstanding	Earned per Sh 1988	1987	Divs. per Sh 1988	1987	Call Price	Price Range 1988	1987
1 Common	No par		[1]118,184,000	[1]$3 34	[1]$3 74	$2 94	$2 86		33⅞- 26⅛	39⅛

[1]Based on avg shs as reported by Co [2]Times over-all charges (after income tax) [3]For additional details, see Houston Lighting & Power Co, appended statement [4]Subject to change, see text

HISTORY

Organized in Tex in Oct. 1976 by Houston Lighting & Power Co (Houston Lighting)

On Jan 14, 1977, pursuant to a merger and corporate restructuring plan, Co became the owner of all of the outstg com stock of Houston Lighting and two of its former subsidiaries, Primary Fuels, Inc and Utility Fuels, Inc In the merger and restructuring, each share of the outstg com. stock of Houston Lighting became one share of Co com. stock In addition, Houston Lighting's outstg. convertible debentures became convertible into Co com stock

In June 1985, created Innovative Controls, Inc a subsidiary which develops and markets high intensity discharge lights driven by electronic ballasts

In Dec 1985, The North American Coal Corp announced that Utility Fuels, Inc, a subsidiary of Co acquired North American's Coals 45% interest in certain lignite reserves near Malakoff, Tx.

In 1986 Co formed KBLCOM Incorporated

In Jan 1987, Co formed Development Ventures, Inc

In Jan 1987, Houston Industries Finance, Inc began purchasing the accounts receivable of HL&P

In Mar 1988, KBLCOM Inc, a subsidiary of Company, acquired the United States cable television interests of Rogers Communications Inc

BUSINESS

Co is a holding company operating through subsidiaries

Houston Lighting and Power Co is engaged in the generation, transmission, distribution and sale of electric energy, serving an area of the Texas Gulf Coast Region, estimated at 5,000 square miles, in which are located Houston (the largest city in Texas) and 156 smaller cities, villages and communities As of December 31, 1988, the total assets and common stock equity of HL&P represented 89% of both the Company's consolidated assets and consolidated common stock equity For the year then ended, the operations of HL&P accounted for 93% of the Company's consolidated net income

Primary Fuels, Inc engages in oil and gas exploration, development and production Company has sold or has agreed to sell Primary's U S Canadian and Argentine operations and is seeking buyers for it's remaining operations located in Greece and Indonesia

Utility Fuels, Inc provides coal and lignite supply services to HL&P Innovative Controls, Inc develops, manufactures and markets high intensity discharge lights

KBLCOM Incorporated serves over 550,000 cable television customers in four states KBLCOM also owns a 50% interest in Paragon Communications, a cable television operating company, serving approximately 735,000 customers

Houston Industries Finance, Inc purchases the account receivable of HL&P

Development Ventures, Inc provides start-up financing for promising small businesses and invests in established funds

PROPERTIES

Through its subsidiary, Houston Lighting & Power Co, Co owns and operates generating facilities with an aggregate nameplate capacity of 13,259,000 kilowatts

Utility Fuels, Inc. owns railroad cars and coal handling facilities used to provide coal supply services to HL&P's W A Parish plant and coal handling facilities at HL&P's Limestone lignite plant. The UFI fleet totals 2,375 railroad cars which comprise 19 trains used for hauling coal

SUBSIDIARIES (wholly-owned)

[1]Houston Lighting & Power Company
KBLCOM Incorporated
Utility Fuels, Inc
Innovative Controls, Inc
Houston Industries Finance, Inc
Development Ventures, Inc

[1]See appended statement

LETTER TO SHAREHOLDERS

Following is the letter to shareholders by Don D Jordan, President and Chief Executive Officer, as it appeared in Co's 1988 Annual Report

To Our Shareholders:

Nineteen-eighty-eight presented both uncertainties and opportunities for Houston Industries, in our core electric utility, business as well as in our quest for growth through diversification We made substantial progress in both areas.

However, our financial results suffered somewhat, primarily as a result of costs incurred by our principal subsidiary, Houston Lighting & Power Company, which were not recovered through electric rates Houston Industries' consolidated earnings were $395 million, or $3 34 per share, in 1988, compared to $435 million, or $3 74 per share, in 1987

Earnings for HL&P were $369 million, or $3 12 per share, in 1988, down from $409 million, or $3 51 per share, a year earlier HL&P has not had an increase in base rates since December 1986 and is not fully recovering the cost of two new generating units placed in service since that time

HI's consolidated earnings also reflected an $8 6 million loss for Primary Fuels, Inc. in 1988, following a $4 5 million profit for our oil and gas subsidiary a year earlier Utility Fuels, Inc, our coal supply subsidiary, reported record earnings of $34 6 million in 1988, an increase from $24 2 million the previous year

Our 1988 earnings were solid in view of factors which are impacting the Company in the short-term, and I am confident that our current actions, such as seeking approval for rates which reflect HL&P's current costs, will improve our long-term financial performance

Construction Ending, Rate Case Pending

Houston Lighting & Power Company achieved several major milestones in completing a power plant construction program, which will ensure a stable, secure electricity supply into the late-1990s HL&P placed the first nuclear unit at the South Texas Project in commercial operation on August 25, 1988 STP Unit 1 is the first operating nuclear unit in Texas In March 1989, HL&P received a full-power operating license for the second STP unit, which is on schedule for commercial operation in mid-1989, and which is the last new generating unit we are building at this time

We are now working to clear the final hurdle associated with the construction of new plant facilities—obtaining regulatory approval to begin recovering our investment through higher electric rates In November 1988, we filed a request for a $432 million base rate increase The request is the first in a three-step rate moderation plan designed to allow HL&P to fully recover the cost of building and operating the new plants, while also softening the impact of higher rates on the local economy

Interim Relief Requested

We do not expect a decision on our rate case until late-1989, and we have asked the Public Utility Commission of Texas to approve the use of deferred accounting for costs associated with STP Unit 1 and Unit 2 at the Limestone lignite plant, which has been in commercial operation since December 1986

If approved as requested, deferred accounting will allow HL&P to seek later recovery of operating and carrying costs for both units from the commercial operation date of STP Unit 1 until rates reflecting those costs take effect. This accounting treatment also would eliminate a drain on HL&P's earnings of approximately $17 million a month, which is resulting from commercial operation of STP Unit 1 without rates which reflect the unit's costs I believe the PUC will recognize our critical need for this interim relief and will approve the use of deferred accounting

Regulation Will Impact Outlook

The South Texas Project is a quality nuclear plant, which was built at a cost that compares favorably with the cost of other nuclear plants built during the same time period I am convinced that STP and the other facilities which HL&P is seeking to include in electric rates will provide substantial long-term benefits to customers. We have prepared a strong rate case to demonstrate these benefits and to document the costs we are seeking to recover However, the outlook for HL&P is highly dependent on the decisions to be made by regulators

Houston Industries has been successful in m[...] taining its financial stability through past peri[...] of uncertainty, and we have provided holders [...] our common stock with uninterrupted quar[...] dividends for 67 consecutive years, both in t[...] of record earnings and in periods of short-[...] financial setbacks We remain committed to pa[...] attractive, stable dividends and would co[...] interrupting that tradition only in the event o[...] extremely adverse rate decision or other [...] which would severely impact the Company

We anticipate that HL&P ultimately will re[...] equitable regulatory treatment for its investm[...] new facilities, and we are looking forward [...] period of lower capital requirements, impr[...] cash flow and more stable earnings for our e[...] utility

Austin Litigation Resumes

I am extremely proud of the progress [...] made in bringing a long era of power plant [...] struction very near to a successful conc[...] However, I am disappointed that one constru[...] related issue remains unresolved We have [...] unable to settle a long-standing legal disput[...] the City of Austin, one of the South Texas P[...] owners

Although we succeeded in reaching an [...] court settlement, which both parties believed [...] in their best interests, we were unable to [...] one condition of the agreement. The sett[...] was contingent on HL&P obtaining a ruling [...] the Public Utility Commission that the agr[...] was in the public interest The PUC re[...] give such a finding and ruled that the issue [...] be considered in future rate proceedings W[...] mately exercised our right to terminate the [...] ment rather than risk future disallowances

Trial of the case began in March 1989 [...] expected to be a lengthy legal process W[...] tinue to regard Austin's claims to be without [...] We have a strong case which will be pr[...] well and we believe our case will be persuasi[...]

HI Narrows Strategic Focus

Houston Industries took a major step [...] growth of it diversified businesses w[...] purchase of the U S cable properties o[...] Communications, Inc The acquisition, [...] closed in March 1989, makes our cable [...] subsidiary, KBLCOM Incorporated, one o[...] largest cable operators in the country

We entered the cable industry in 1986 b[...] its operating similarities to our core electr[...] business We are expanding in that [...] because our earlier cable venture has exc[...] expectations, particularly in terms of the [...] which we've enjoyed in the value of our [...] ment. The properties we acquired from R[...] high-quality systems serving attractive [...] markets

We are building long-term growth [...] through our diversified business, and w[...] long-term perspective in evaluating ac[...] Because it takes a number of years to b[...] ing a profit in the cable industry, we [...] that the Rogers acquisition will prod[...] earnings dilution in the early years of o[...] However, cable television enjoys growing [...] demand and significant untapped source[...] nue After the startup period, we exp[...] steady cash flows

The same long-term strategic planning [...] to HI's expansion in the cable indu[...] resulted in our decision to leave the o[...] industry In early 1989, we accepted off[...] approximately $270 million for the U.S. [...] and Argentine operations of Primary F[...] our oil and gas subsidiary We are co[...] explore opportunities to sell PFI [...] located in Indonesia and Greece

Our decision to expand in the cable in[...] leave the oil and gas industry is con[...] our diversification strategy of focusin[...] nesses similar to our core business, wh[...] the same types of management exp[...] gained in the electric utility industry

We remain committed to selective di[...] as an avenue for future growth Ho[...] non-utility business activities could b[...] curtailed if the Securities and Exchang[...] sion adopts a proposed rule which wo[...] tially limit diversification by intrastate [...] ing companies, including Houston In[...] are monitoring this proposal and will [...] right to select a balance of regulated an[...] lated businesses to benefit our investors.